Before the
Federal Communications Commission
Washington, D. C. 20554

In the Matter of	)	
	)	
Amendment of Parts 32 and 64 of the Commission's Rules to Account for Transactions Between Carriers and Their Nonregulated Affiliates	)	CC Docket No. 93-251

REPLY COMMENTS
OF THE
UNITED STATES TELEPHONE ASSOCIATION

The United States Telephone Association (USTA) respectfully submits its reply to comments filed December 10, 1993 in the above-referenced docket.

In its comments, USTA opposed the Commission's proposed rules to increase regulatory requirements for affiliate transactions. USTA explained that the proposed rules are burdensome, costly and unnecessary and have not been shown to serve the public interest. The vast majority of commenting parties agreed with USTA.

The majority of commenting parties agreed that the Commission provided no justification to support its proposed rule changes. "The genesis of the NPRM is a mystery...without giving any factual explanation other than pure speculation, [it] proposes to scrap the affiliate transaction rules which the Commission and the industry have worked so hard to implement".[1] "[T]here has been no demonstration that the current rules, combined with the FCC's active program of enforcement, do not

[1]Southwestern Bell at 1.

provide sufficient protection for the ratepayer. Surely the adoption of far more burdensome regulations must be grounded on identified problems that have arisen rather than a feeling that present rules 'may not be optimal'."[2]

> No evidence suggests that consumers have been or will be harmed under the present rules, or how carriers have been imprudent. For example, no one has identified either the number of transactions or the levels of dollars which may have had to be reclassified out of regulation, or how much consumers may have overpaid since the current rules were put in place. There is no evidence that the independent auditor requirements or attest audits have been ineffective, or that the Commission's own review of auditor workpapers has uncovered overcharges to consumers, or that LECs have acted imprudently. New rules, especially the very complex, costly and contentious ones proposed, should not be adopted without a documented or demonstrated need. No such documentation or demonstration has been made.[3]

Even those parties supporting the proposed rule changes do not provide any evidence that the additional regulatory burdens are justified.[4] These parties simply repeat many of the same unsupported speculation and groundless allegations that they voiced during Commission consideration of the Joint Cost Order. In fact, one party supporting the proposed rules recommends "that the Commission provide more details and citations to support its conclusions that the current affiliate transaction rules need to be greatly strengthened."[5]

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[2]GTE at 10.

[3]Southern New England Telephone Company (SNET) at 2.

[4]See, for example, comments of MCI, International Communications Association (ICA) and Information Technology Association of America (ITAA).

[5]ICA at 5.

In seeking to modify its existing rules, the Commission must provide a reasoned analysis supporting the modification, which should include some justification for the proposed change.[6] As the commenters point out, the Commission has failed to provide a sufficient basis to justify adoption of the proposed rules changes. The record established in the comments show that the current rules are more than sufficient to protect against improper cross subsidy and that the implementation of incentive regulation and the advent of steadily increasing competition have reduced the need for the additional regulatory scrutiny proposed by the Commission. The record also shows that the proposed rules would impose a costly and burdensome administrative process on exchange carriers which threatens the economies of scale currently available to benefit ratepayers. "Thus, when the Commission balances the costs imposed by its proposed rules against the fact that its current rules already meet its goals, the Commission should easily conclude that it is in the public interest to maintain its current rules."[7]

Perhaps the most compelling comments were made by Coopers & Lybrand, a public accounting firm that conducts audits of Tier 1

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[6]See, Sierra Club v. Clark, 755 F.2d 608 (8th Cir. 1985) and Gr. Boston Television Corp. v. FCC, 444 F.2d 841 (D.C. Cir. 1970). The Court stated that in departing from prior practices, the agency "must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored, and if any agency glosses over or swerves from the prior precedents without discussion it may cross the line from the tolerably terse to the intolerably mute."

[7]Ameritech at 6.

carriers pursuant to the Commission's rules. The comments state that "[t]he adoption of this proposed change [to the fully distributed cost 'residual rule'] will add substantial difficulty to the carrier's affiliate transaction process and complexity and subjectivity to the audit process thereby diminishing the enforcement mechanism that the FCC currently has in place."[8] The comments go on to detail the problems with the proposed use of estimated fair market value, including the difficulty in identifying comparable transactions in the market and the inherent subjectivity of estimated fair market value and the large volume of service transactions that would be subject to the estimated fair market value process. "The proposed rules move away from those criteria [in the Joint Cost Reconsideration Order], create a complete new layer of work to value services, make it far more difficult for companies to determine whether they are in compliance with rules, add complexity and subjectivity to the audit process and render the company and auditor conclusions subject to continued debate because the market valuation of services adds substantial subjectivity to the rules".[9]

As noted above, those comments in support of the Commission's proposal offer only speculation to justify adopting the proposed rules. Even these comments recognize certain deficiencies in the Commission's proposals which render them

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[8]Coopers & Lybrand at 1.

[9]Id, at 4.

arbitrary or burdensome. Therefore, USTA will only specifically address several issues raised by MCI and ICA.

MCI contends that the use of prevailing company price is "unchecked".[10] That statement is incorrect. The Commission has not reported any deficiencies in any company's use of prevailing company price. Further, such prices are scrutinized by the Commission under the current rules. MCI even admits that the Commission's 75 percent threshold test to permit continued use of prevailing company price is arbitrary.[11] The Commission's proposed test is also unnecessary. "It is highly unlikely that an affiliate could successfully achieve substantial sales to nonaffiliates if its price exceeded market value."[12] Any restriction on the use of prevailing company price will seriously disadvantage exchange carriers and their affiliates and distort the marketplace. Given the arbitrariness of the Commission's alternative and the lack of any evidence that the current rules are ineffective, the existing rules should not be altered. Even if a certain percentage could be validated, according to a study filed by AT&T, "a 75 percent threshold is far higher than any economic principles or theory would justify."[13]

ICA, while supporting the Commission's proposals, recognizes that the new rules would be burdensome and suggests that the

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[10]MCI at 5.

[11]Id. at 6.

[12]BellSouth at 23.

[13]AT&T at 18.

Commission could take a more streamlined approach than the detailed item-by-item approaches discussed in the Notice.[14] ICA's suggestion that exchange carriers be required to list in their CAMs each section and subsection of a tariff involving transactions with affiliates, even if the transaction is based on an ICB offering, should be rejected.[15] All federal tariffs must be filed with the Commission and are subject to Commission review and approval. There is no need for any further review of tariffs in the CAM process.

ICA's recommendation that exchange carriers specify the Uniform System of Accounts for services using an estimated fair market valuation fails to describe any associated benefit and should also be rejected.[16] ARMIS and the audit process are sufficient to ensure carrier compliance.

As noted in its comments, USTA agrees with AT&T's statement that "many of the Commission's specific proposals are thoroughly impractical, either because they are virtually impossible to implement as currently proposed, or because the costs of creating the systems necessary to implement the rules would be staggering."[17] For example, AT&T explains that the Commission's approach to chain transactions is simply unworkable as applied to many affiliate transactions. "[I]t is often the case that the

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[14]ICA at 11.

[15]Id. at 10.

[16]ICA at 14.

[17]AT&T at 15.

final, transferred product in an affiliate transaction is a sophisticated device, such as a switch, having a large number of component parts. These parts were in all likelihood themselves transferred among affiliates prior to incorporation into the final product. The Commission's proposed rules would require AT&T to trace every nut and bolt incorporated into the switch, through a chain of transfers, to derive a cost basis for the final product and for every intermediate product. The expense of such an undertaking would obviously be staggering."[18]

The Commission has failed to demonstrate how the public interest would be better served through its proposed rule changes. Based on the record established in the comments, USTA urges the Commission not to adopt the proposed additional regulatory requirements for affiliate transactions and to continue to rely on the current rules which have been successful in protecting ratepayers against any improper cross subsidy.

Respectfully submitted,

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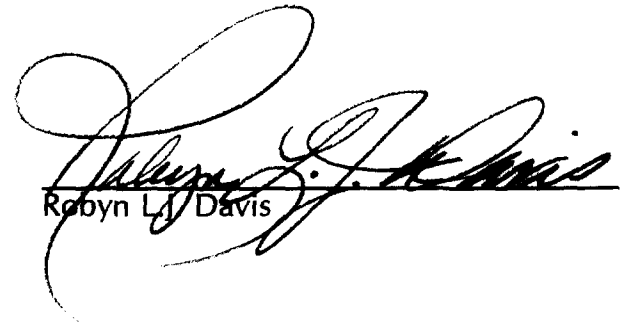
[18]AT&T at 17.

CERTIFICATE OF SERVICE

I, Robyn L.J. Davis, do certify that on January 10, 1994 copies of the Reply Comments of the United States Telephone Association were either hand-delivered, or deposited in the U.S. Mail, first-class, postage prepaid to the persons on the attached service list.



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